Coach Creates a Path for Other U.S. Companies to List in Hong Kong

Fried Frank advised leading accessories brand Coach in connection with its December 1st listing of Hong Kong depositary receipts (HDRs) representing Coach common stock on the Hong Kong Stock Exchange. The listing makes Coach the first company incorporated in the United States to list in Hong Kong. In connection with the listing, Coach also obtained a no-action letter from the SEC Staff on November 28th which granted relief from certain of the requirements of Regulation S under the Securities Act of 1933 (the 1933 Act). Approval of the listing by the Hong Kong regulators, as well as the SEC Staff's decision, serve as important precedents for other U.S. companies considering following in Coach's footsteps.

Background of the Coach Listing

In recent years, a number of international brands have sought listings in Hong Kong to tap into the investor base in Asia and to gain increased visibility among the growing middle class in China who use their products. Examples include L'Occitane, Prada and Samsonite, all of which sought primary listings in Hong Kong as part of their initial public offerings. Certain other international companies have also completed secondary listings in Hong Kong including Brazilian mining company Vale which completed a secondary listing without a capital raise to increase its profile in China. Others currently rumored to be in the queue for Hong Kong listings include Graff Diamonds and Louis Vuitton Moet Hennessy.

Seeking to increase its presence in Asia, Coach completed a secondary listing of HDRs by way of introduction on the Hong Kong Stock Exchange. A listing by way of introduction does not involve raising capital and is similar to a sponsored Level II American depositary receipt program in the United States. HDRs are similar to American depositary receipts and global depositary receipts in that they represent underlying common or ordinary shares deposited with a depositary. The listing also permits a Hong Kong dollar denominated security to be accessible to Asian investors during Hong Kong trading hours. Coach's primary listing continues to be the New York Stock Exchange.

Why Depositary Receipts?

Hong Kong introduced its depositary receipt framework in July 2008. Since that time, the Hong Kong Stock Exchange has been actively courting overseas companies to come to Hong Kong via a depositary receipt listing. Coach's listing is the third such listing since the implementation of the framework and the first by a company incorporated in the United States.

Pursuing a depositary receipt structure in Hong Kong, as compared to a common stock structure, may be driven by a number of factors similar to those considered when pursuing depositary receipt programs elsewhere. These factors include, among other things:

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• the ability to re-size the security's price to appeal to investors in the secondary listing jurisdiction;
• prohibitions on maintaining an overseas share register;
• ease of administration in terms of time and cost when moving securities between two jurisdictions; and
• allowing payment of dividends in local currency.

The Hong Kong Stock Exchange also recently encouraged overseas companies to use HDRs, particularly in light of the current nature of its clearing system.2

Acceptance of Overseas Incorporated Companies in Hong Kong

The listing criteria in Hong Kong provide that companies incorporated in Hong Kong, China, Bermuda and the Cayman Islands may list on the Hong Kong Stock Exchange. The Hong Kong Stock Exchange, along with the Hong Kong Securities and Futures Commission, also consider applicants incorporated in other jurisdictions so long as the applicants can show that their home jurisdictions have at least equivalent standards of shareholder protection as compared to those in Hong Kong. For purposes of this analysis, the Hong Kong regulators published a roadmap in March 2007, known as the Joint Policy Statement, which sets out various shareholder protection matters under the Hong Kong Companies Ordinance against which an applicant is required to compare equivalency of its home jurisdiction's protections. Where the frameworks deviate on particular points, the Hong Kong regulators have permitted workarounds. A number of jurisdictions have been approved under this process including Australia, Brazil, the British Virgin Islands, certain provinces of Canada, California, Cyprus, France, Germany, Guernsey, Isle of Man, Italy, Japan, Jersey, Luxembourg, Singapore, and the United Kingdom.

Recently, the Hong Kong Stock Exchange stated that they and the Hong Kong Securities and Futures Commission were re-examining the Joint Policy Statement and whether the Hong Kong Companies Ordinance was the appropriate regulatory benchmark for the shareholder protection equivalency analysis.3 Further, based on the experience of Coach’s listing, it appears that the Hong Kong regulators may be moving toward a case-by-case analysis for certain applicants.

Reconciling Regulatory Regimes

A secondary listing in Hong Kong (as compared to a primary listing) permits the applicant to obtain a number of waivers from compliance with the Hong Kong listing rules, takeovers code and securities-related ordinances. These waivers focus on, among other things, a balancing of investor expectations with the burden of an applicant of having to comply with two regulatory frameworks where the trading is predominantly in the home market and the primary listing involves a regulatory framework with acceptable investor protections. Coach, as a U.S. domestic reporting issuer, is the first company subject to the full U.S. regulatory regime (unlike a foreign private issuer) that has completed such waiver process. The waivers obtained by Coach include:

• the ability to use periodic reports filed in the United States to fulfill similar reporting requirements in Hong Kong;
• waivers from Hong Kong’s shareholder approval and disclosure requirements for related party transactions (known as “connected transactions”) and certain share issuances and acquisitions and disposals (known as “notifiable transactions”) provided that the regulatory framework in the United States is followed;

the ability to use Section 16 filings and Section 13 filings under the Securities Exchange Act of 1934 to fulfill similar security ownership filing requirements in Hong Kong; and

an exemption from the Hong Kong takeovers code, which provides for a regulatory regime quite different from the United States, and, in Coach's case, may be the first such exemption granted to a company incorporated in the United States.

Liquidity Arrangements

In the context of a listing where there is no capital raise, the Hong Kong Stock Exchange expects adequate measures to be in place to ensure that there is sufficient liquidity in the securities. These liquidity arrangements are precautionary measures designed to help facilitate a liquid and orderly market for the securities for a limited initial period following the listing. For example, as in Coach's listing, there may be a designated dealer who borrows shares from the open market to create an inventory of HDRs thereby acting as a conduit to allow some of the liquidity in the primary trading market to migrate to the secondary trading market. These measures may supplement any voluntary movement by existing securities holders from one market to the other.

U.S. Securities Laws Considerations

In order to avoid any concerns regarding compliance with the registration requirements of the 1933 Act, Coach and the depositary sought no action relief from the SEC Staff such that they could take advantage of the Regulation S safe harbor. Among other things, the Regulation S safe harbor permits U.S. companies to make offerings of equity securities abroad to foreign investors without registration under the 1933 Act.

As Coach is a U.S. domestic issuer, the requirements of Category 3 of the Regulation S safe harbor may be applicable to the issuance and secondary trading of the HDRs. The Category 3 requirements of the Regulation S safe harbor provide, in part, that the HDRs cannot be sold into the United States or to a U.S. person or for the account or benefit of a U.S. person prior to the expiration of a six month distribution compliance period and purchasers of HDRs may not engage in hedging transactions except in compliance with the 1933 Act.

As a result of the manner in which securities are traded and settled on the Hong Kong Stock Exchange, strict compliance with the following Category 3 requirements of Regulation S would not be feasible in connection with the issuance and secondary trading of the HDRs on the Hong Kong Stock Exchange:

- purchaser certification, purchaser agreement regarding resale, legending and stop-transfer requirements (Rule 903(b)(3)(iii)(B) of Regulation S);
- distributor notification requirements (Rule 903(b)(3)(iv) of Regulation S); and
- dealer notification requirements (Rule 904(b)(1)(ii) of Regulation S).

These requirements would not be possible as book-entry trading was expected to be the primary means for trading in the HDRs.

The no-action relief provided by the SEC Staff permits Coach and the depositary to satisfy the above-mentioned requirements of Category 3 of the Regulation S safe harbor by implementing alternative restrictions and procedures, including:

- disclosure in Coach's Hong Kong listing document (which is similar to a U.S. style prospectus) of deemed representations regarding a purchaser's non-U.S. status and agreements regarding restrictions on resale and hedging;

- the Hong Kong Stock Exchange's agreement to advise all exchange participants that:
  - no exchange participant may execute a transaction in the HDRs if such exchange participant has knowledge that the buyer is a U.S. person or is acting for the account or benefit of a U.S. person;
to the extent an exchange participant is purchasing HDRs on behalf of its customer that is not an exchange participant, the exchange participant making such purchase must make reasonable efforts to ascertain that its customer is not a U.S. person and is not acting for the account or benefit of a U.S. person; and
exchange participants must implement measures designed to assure reasonable compliance with the foregoing requirements;
• inclusion of a restrictive legend on any certificated HDRs;
• identification of the HDRs in the CUSIP database as subject to the restrictions of Regulation S;
• Coach's agreement to include a statement that the HDRs have not been registered under the 1933 Act and are subject to the restrictions of Regulation S in any information provided by Coach to publishers of publicly-available databases (e.g., BLOOMBERG) about the terms of any issuance of the HDRs;
• the Hong Kong Stock Exchange's agreement to:
  o add an "RS" identifier to Coach's full name on its website (i.e., Coach, Inc. -RS) and in the HDRs' short name (i.e., COACH-DRS-RS);
  o assign Coach a numeric stock code within a newly established range reserved for U.S. companies that have restricted HDRs; and
  o publish explanations of the above-mentioned "RS" identifier and the numeric stock code;
• the Hong Kong Stock Exchange's agreement to advise all exchange participants that trade confirmations should include the HDRs' short name, including the "RS" identifier, and the numeric stock code;
• covenants by the depositary and Coach in the deposit agreement that no Hong Kong depositary shares (evidenced by the HDRs) in physical certificated form, for so long as they contain the Regulation S legend thereon, may be transferred by, or on behalf of, the depositary without a favorable opinion of counsel or other assurance in the depositary's discretion that the transfer complies with the 1933 Act; and
• Coach's agreement to provide notification of the Regulation S status of its securities in shareholder communications, such as annual reports, periodic interim reports, dividend notices and its notices of shareholder meetings.

With this no-action letter, the Hong Kong Stock Exchange now has procedures in place that other U.S. listed, domestic companies may find useful. Further, while the no-action letter is limited to transactions involving no capital raise, the SEC Staff has provided prior relief involving non-reporting U.S. companies doing capital raising exercises on foreign exchanges. Accordingly, the ability of U.S. companies to do capital raises via an HDR program may be feasible.

Conclusion
As noted above, Coach's listing has created a path for others to follow. As with any transaction, there are a number of other issues to consider or that may arise in the context of a particular applicant. Our team is available to discuss these listings with your company or organization in more detail and assist with any structuring issues.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its contents. If you have any questions about the contents of this memorandum, please call your regular Fried Frank contact or the attorneys listed below:

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